

## Message Text

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ACTION ARA-10

INFO OCT-01 ISO-00 CIAE-00 DODE-00 PM-03 H-01 INR-05 L-02

NSAE-00 NSC-05 PA-01 RSC-01 PRS-01 SP-02 SS-15

USIA-06 EB-04 AID-05 /062 W  
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R 071315Z NOV 74

FM AMEMBASSY LIMA

TO SECSTATE WASHDC 2623

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EO 11652: N/A

TAGS: EGEN, PE

SUBJECT: FINANCE MINISTER DISCUSSES PERUVIAN ECONOMY

1. SUMMARY: IN A NATIONALLY TELEVISED SPEECH OCTOBER 31, MINISTER OF ECONOMY AND FINANCE, GENERAL AMILCAR VARGAS GAVILANO PORTRAYED THE PERUVIAN ECONOMY AS SOUND DESPITE SERIOUS BUFFETING FROM EXTERNAL INFLATION. THE SPEECH CONTAINED NO SURPRISES AND WAS DESIGNED IN CONTENT AND STYLE TO CONVEY AN IMPRESSION OF PROFESSIONAL COMPETENCE ON THE PART OF THE NEW TEAM AT THE MINISTRY AND TO ALLAY CONCERN ABOUT THE ABILITY OF PERU, AND ITS ECONOMIC MANAGERS, TO CONTROL ECONOMIC DEVELOPMENTS. SOME UNCERTAINTY REMAINS, HOWEVER, SINCE THE SPEECH DEALT ALMOST EXCLUSIVELY, ELBEIT SUPERFICIALLY, WITH THE SUCCESSES OF 1974 AND FAILED TO ACCORD ADEQUATE RECOGNITION TO THE DIFFICULTIES FACING THE ECONOMY. THE MINISTER PROMISED TO MEET FREQUENTLY WITH THE PRESS TO KEEP IT INFORMED OF SPECIFIC ECONOMIC PROBLEMS AND DEVELOPMENTS. THE SPEECH CONTAINED THE USUAL EXHORTAION FOR POPULAR SUPPORT OF THE REVOLUTION. SURPRISINGLY, THERE WAS NO MENTION OF THE EPSA SCANDAL (LIMA 8955) NOR OF THE SHORTAGES OF BASIC FOOD ITEMS WHICH REPORTEDLY HAVE BEEN OCCURRING PARTIALLY DUE TO EPSA MISMANAGEMENT. END SUMMARY.

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2. FOLLOWING ARE THE PRINCIPAL ECONOMIC STATISTICS PRE-

SENTED IN THE SPEECH TOGETHER WITH THE EMBASSY'S COMMENT  
ON SELECTED IMES (ALL FIGURES ARE FOR CY74 UNLESS OTHER  
WISE INDICATED):

A. GROWTH - REAL GROWTH IN GNP WILL REACH 6.3 PERCENT  
FOR 1974, LED BY THE FISHING SECTOR (52 PERCENT), CONSTRU-  
TION (20 PERCENT) AND MANUFACTURING (8 PERCENT). THE  
AGRICULTURAL SECTOR WILL SHOW ONLY SLIGHT GROWTH (1.2 PER-  
CENT).

B. DEMAND - PRIVATE CONSUMPTION SPENDING WILL INCREASE  
BY 10 PERCENT, PUBLIC CONSUMPTION BY 1 PERCENT, PUBLIC IN-  
VESTMENT BY 37 PERCENT, PRIVATE INVESTMENT BY 17 PERCENT,  
AND TOTAL INVESTMENT BY 25 PERCENT. COMMENT: THE PUBLIC  
CONSUMPTION FIGURE IS CONSIDERABLY UNDERESTIMATED SINCE  
GOP EMPLOYMENT AND SALARIES HAVE INCREASED SIGNIFICANTLY.  
THIS DISCREPANCY WAS DEMONSTRATED WITHIN THE BODY OF THE  
MINISTER'S SPEECH IN A SEPARATE TABLE WHICH SHOWS CURRENT  
EXPENDITURES OF THE GOP UP 44 PERCENT IN THE PRESENT BIENNIAL  
BUDGET PERIOD.

C. EMPLOYMENT - UNEMPLOYMENT IN THE LIMA/CALLAO  
AREA WILL FALL FROM 7.7 PERCENT TO 6.5 PERCENT BY THE  
END OF 1974. COMMENT: ALTHOUGH IT IS POSSIBLE THAT EMPLOYMENT INCREASE  
S EXCEEDED NEW ADDITIONS TO THE LABOR  
FORCE DURING THE PAST YEAR, UNDEREMPLOYMENT (WHICH WAS  
NOT MENTIONED BY THE MINISTER) AND UNEMPLOYMENT REMAIN  
SERIOUS SOCIAL PROBLEMS FOR THE GOP, WITH A COMBINED RATE  
IN EXCESS OF 30 PERCENT.

D. PRICES - GOP SUBSIDIES AND PRICE CONTROLS HAVE  
HELD PRICES TO AN INCREASE OF ONLY 14 PERCENT OVER THE  
FIRST NINE MONTHS OF 1974 DESPITE SEVERE EXTERNAL PRES-  
SURES. COMMENT: ON AN ANNUAL BASIS THE INFLATION RATE WOULD THUS BE  
19 PERCENT, PROBABLY UNDERSTATING THE ACTUAL ANNUAL RATE BY  
FIVE PERCENTAGE POINTS.

E. CENTRAL GOVERNMENT BUDGET - BOTH EXPENDITURES AND  
RECEIPTS WILL INCREASE BY 51 PERCENT, WITH THE RESULTING  
DEFICIT EQUAL TO 1.9 PERCENT OF TOTAL RECEIPTS. TAXES WILL  
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INCREASE BY 39 PERCENT. COMMENT: THE MINISTER DEFINED  
THE BUDGET DEFICIT AS TOTAL EXPENDITURES MINUS TOTAL RE-  
CEIPTS, DISINGENUOUSLY NEGLECTING TO MENTION THAT 31 PER-  
CENT OF TOTAL RECEIPTS ARE BORROWINGS TO FINANCE THE EX-  
PENDITURES, INCLUDING FOREIGN LOANS.

F. BALANCE OF PAYMENTS - EXPORTS WILL INCREASE BY  
36 PERCENT, IMPORTS BY 95 PERCENT, RESULTING IN A TRADE

DEFICIT OF \$449 MILLION. GROSS LONG-TERM CAPITAL INFLOW WILL BE \$881 MILLION (NET \$430 MILLION). OVERALL BALANCE OF PAYMENTS WILL SHOW A SURPLUS OF \$13 MILLION. COMMENT: THE NET BASIC BALANCE (TRADE AND SERVICES DEFICIT MINUS NET LONG TERM CAPITAL INFLOW) SHOWS A DEFICIT OF \$446 MILLION, A FACT CONTAINED IN THE STATISTICAL TABLES BUT NOT MENTIONED BY THE MINISTER. THIS DEFICIT WILL BE COVERED BY SHORT-TERM CREDIT INFLOWS (WHICH, IN THE EMBASSY'S VIEW, MAY BE INTERPRETED AS A POTENTIAL SERIOUS WEAKNESS IN THE PERUVIAN ECONOMY) AND ERRORS AND OMISSIONS.

G. FOREIGN DEBT - AS OF SEPTEMBER 30, OUTSTANDING DEBT \$1,910 MILLION. DEBT INCREASED BY 667 PERCENT DURING 1960-1968 BUT ONLY 159 PERCENT DURING 1968 TO PRESENT. DEBT SERVICE TO EXPORT RATIO AFTER REFINANCING IS 13.2 PERCENT.

H. RESERVES - NET INTERNATIONAL RESERVES WERE \$539 MILLION AS OF OCTOBER 21. COMMENT: THIS FIGURE, WHICH PRESUMABLY REPRESENTS GROSS RESERVES MINUS SHORT-TERM LIABILITIES SEEMS EXAGGERATED AND IF ACCURATE, IMPLIES AN INCREASED LONG-TERM DEBT.

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USIA-06 EB-04 AID-05 /062 W

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R 071315Z NOV 74

FM AMEMBASSY LIMA

TO SECSTATE WASHDC 2624

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4. COMMENT: VARGAS' SPEECH BORE A STRIKING RESEMBLANCE TO THOSE OF FORMER FINANCE MINISTER GENERAL MORALES BERMUDEZ WHEN HE OCCUPIED THAT POST, ALTHOUGH IT WAS LESS CANDID IN FACING UP TO PRESSING PROBLEMS. DATA SEEMED TO BE PRESENTED TO OBFUSCATE RATHER THAN CLARIFY ISSUES. VARGAS TOOK PAINS

TO CAUTION AGAINST MISINTERPRETATION OF THE DATA, AN OBVIOUS REFERENCE TO RECENT PUBLISHED STATEMENTS IN THE OPPOSITION PRESS QUESTIONING THE SIZE OF THE EXTERNAL PUBLIC DEBT. NOTWITHSTANDING THE ADVANCE PUBLICITY GENERATED ABOUT THE SPEECH, IT CONTAINED NO INDICATION OF ANY NEW POLICY MEASURES, AND THE MINISTER WENT OUT OF HIS WAY TO DEFEND THE GOVERNMENT'S PRICE SUBSIDIES POLICY. WHILE AGREEING WITH THE GENERAL TONE AND THRUST OF THE SPEECH, WE BELIEVE IT WAS A LESS THAN CANDID ASSESSMENT OF THE COST TO THE GOP OF ITS SUBSIDIES PROGRAM. IT ALSO AVOIDED AN EXPLANATION OF HOW GOP MAY BE REQUIRED TO RELAY HEAVILY ON SHORT-TERM FINANCING OF ITS BALANCE OF PAYMENTS IT AS EXPECTED PERU CONTINUES TO RUN LARGE MERCHANDIZE TRADE DEFICITS. IN SUM, WHILE VARGAS ATTEMPTED TO PAINT A GENERALLY POSITIVE PICTURE, THE ISSUES HE OBFUSCATED OR IGNORED WILL CONTINUE TO PLAGUE PERU IN THE FUTURE AND COULD WELL POSE SOME HARD CHOICES FOR THE MINISTER AND THE GIP IN THE NEAR TERM.  
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